MULTIMEDIA UNIVERSITY

STUDENT ID NO

MULTIMEDIA UNIVERSITY

FINAL EXAMINATION

TRIMESTER 2, 2015/2016

BFN3084 – INTERNATIONAL FINANCE

(All sections / Groups)

4th MARCH 2016
9am-11am
(2Hours)

INSTRUCTIONS TO STUDENTS

1. This Questions paper consists of 3 pages with 4 Questions only.
2. Attempt **ALL** questions. All questions carry equal marks and the distribution of the marks for each question is given.
3. Please write all your answers in the Answer Booklet provided.

QUESTION 1

(a) Suppose that the treasurer of Cyberspace X Ltd. has an extra cash reserve of $100,000,000 to invest for six months. The six-month interest rate is 8 percent per annum in the United States and 7 percent per annum in Germany. Currently, the spot exchange rate is €1.01 per dollar and the six-month forward exchange rate is €0.99 per dollar. The treasurer does not wish to bear any exchange risk. Where should he invest to maximize the return? (10 marks)

(b) Explain the difference in the translation process between the monetary/nonmonetary method and the temporal method. (7 marks)

(c) Discuss the advantages and disadvantages of the gold standard. (8 marks)

(Total: 25 marks)

QUESTION 2

(a) A firm holds an asset in Amsterdam, Netherland and faces the following scenario:

	State 1	State 2	State 3	State 4
Probability	25%	25%	25%	25%
Spot rate	$1.20/€	$1.10/€	$1.00/€	$0.90/€
P^*	€1500	€1400	€1300	€1200
P	$1,800	$1,540	$1,300	$1,080

In the above table, P^* is the euro price of the asset held by the U.S. firm and P is the dollar price of the asset.

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(i) Compute the exchange exposure faced by the U.S. firm. (12 marks)

(ii) What is the variance of the dollar price of this asset if the U.S. firm remains unhedged against this exposure? (2 marks)

(iii) If the U.S. firm hedges against this exposure using the forward contract, what is the variance of the dollar value of the hedged position? (3 marks)

(b) Discuss the process of bringing a new international bond issue to market. (8 marks)

(Total: 25 marks)

QUESTION 3

(a) Lisbon Ltd.'s cash flows in Portugal as follows.

Year	Cash Flows
Year 0	- €70,000
Year 1	€150,000
Year 2	-€90,000

The current exchange rate is $1.50 = €1.00. The inflation rate in the U.S. is 6 percent and in the euro zone 2 percent. The appropriate cost of capital to a U.S.-based firm for a domestic project of this risk is 8 percent.

(i) Find the euro-zone cost of capital to compute the dollar-denominated NPV of this project. (4 marks)

(ii) Calculate the dollar cash flows to compute the dollar-denominated NPV of this project. (12 marks)

(b) Briefly discuss **THREE (3)** types of risks that to be considered by currency swap dealer. (9 marks)

(Total: 25 marks)

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QUESTION 4

(a) James Ingrame specializes in cross-rate arbitrage. The following spot rates are:

SFr1.5971/$

AUD$1.8215/$

AUD$1.1440/SFr

(i) Ignoring transaction costs, does James Ingrame have an arbitrage opportunity based on these quotes? (5 marks)

(ii) If there is an arbitrage opportunity, what steps would he take to make an arbitrage profit, and how he would profits if he has $1,000,000 available for this purpose? (12 marks)

(b) Differentiate between floating-rate notes and bond with equity warrants. (8 marks)

(Total: 25 marks)

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